



Economic and Social Council

Distr
GENERAL

E/1996/48
1 April 1996

ORIGINAL: ENGLISH

Substantive session of 1996
24 June-26 July 1996
Item 7 of the provisional agenda*

REGIONAL COOPERATION IN THE ECONOMIC, SOCIAL AND RELATED FIELDS

Summary of the survey of economic and social conditions
in Asia and the Pacific, 1996

SUMMARY

Based on the detailed analysis in the Economic and Social Survey of Asia and the Pacific 1996, the document provides an overview of recent economic performance and policy reforms in the economies of the ESCAP region in the light of major developments in the world economy. It also examines two issues of significant concern: enhancing the role of the private sector in economic development and the role of public expenditure in the provision of social services.

The ESCAP region has benefited from several positive developments in the international economy. World output recovered significantly in 1994 following the recession of the early 1990s and registered a growth rate of 2.6 per cent in 1995. The volume of world trade, which grew at 9.5 per cent in 1994, the fastest rate in many years, was followed by a further expansion of 7 per cent in 1995. The region received a considerable share of accelerating flows of private capital, including foreign direct investment. However, there are some concerns, including the declining trend in official development assistance, which plays a substantial role in financing development in a large number of disadvantaged economies.

A combination of favourable developments and sustained domestic policy reforms enabled the developing ESCAP region to record a strong growth performance in 1995, averaging 7.8 per cent. As usual, there has been considerable divergence among countries. The growth rates achieved by most of

* E/1996/100; to be issued.



the least developed countries and island economies remained well below the regional average, while negative growth persisted in the Central Asian republics.

In most countries, the policy stance remained focused on liberalization and deregulation. In varying degrees, the reforms have sought to bring about greater openness in foreign trade, investment and financial sector policies, to increase domestic savings and investment, to maintain price stability, to reduce fiscal deficits and to encourage the private sector to play a greater role. The reform measures have brought to the fore new policy challenges, particularly for the management of key macroeconomic variables such as price level, interest rate, money supply and exchange rate.

Enhancing the role of the private sector in development has been a cornerstone of reform programmes. Towards that end, Governments have tried to strengthen the legal framework for private sector transactions. They have introduced fiscal reforms with the aim of reducing the tax burden for the private sector, liberalizing and deregulating the financial sector so as to increase the access of the private sector to loanable funds at market-determined interest rates. They have set up institutional mechanisms for incorporating private sector concerns in policy-making and they have provided support for the development of small and medium-sized enterprises. The analysis draws attention to the need for further improvements in the legal framework for property rights, enforcement of contracts, competition policies and synergy among measures of support for small and medium-sized enterprises.

While promoting the private sector, the countries in the region have continued to emphasize the role of the public sector in the provision of social services. In most countries, the proportion of public expenditure allocated to social sectors has exceeded 20 per cent and there have been considerable improvements in the field of education, health, water supply and sanitation over the past decade. However, there are several issues to which greater attention needs to be paid. Those relate, *inter alia*, to equity in the provision of services between income classes, regions and gender, cost-effectiveness in the delivery of services, a mobilization of greater resources for the social sector as well as intra-sectoral priorities in the allocation of resources, improvements in the quality of services, and the closer involvement of the private sector, non-governmental organizations and local communities in the delivery of services, as well as establishing and maintaining facilities.

The Commission may wish to urge member Governments to take into account the analysis contained in the present document and in the Economic and Social Survey of Asia and the Pacific 1996 in formulating their national policies. The Commission may also wish to recommend further studies on comparative experience in (a) economic management in the new environment of international openness, competitiveness and the greater role of the private sector; and (b) policies to improve the equity, quality and cost-effectiveness of social services.

CONTENTS

	<u>Paragraphs</u>	<u>Page</u>
I. WORLD ECONOMIC DEVELOPMENTS AND THE ESCAP REGION	1 - 11	4
II. MACROECONOMIC PERFORMANCE AND POLICIES IN THE ESCAP REGION	12 - 27	6
III. INTERNATIONAL TRADE AND BALANCE OF PAYMENTS	28 - 33	13
IV. ENHANCING THE ROLE OF THE PRIVATE SECTOR IN DEVELOPMENT	34 - 48	14
V. THE ROLE OF PUBLIC EXPENDITURE IN THE PROVISION OF SOCIAL SERVICES	49 - 58	18

Tables

1. Selected economies of the ESCAP region: growth rates and inflation, 1993-1995	7
2. Selected economies of the ESCAP region: forecasts of growth rates of gross domestic product and inflation, 1996-1997 ..	10

I. WORLD ECONOMIC DEVELOPMENTS AND THE ESCAP REGION

1. World economic recovery, which strengthened in 1994, stayed on course in 1995. The rate of growth in world output, in fact, accelerated slightly in 1995 to register 2.6 per cent compared with 2.5 per cent in 1994. Among the industrialized countries, the average rate of economic growth in the European Union accelerated from 2.6 per cent in 1994 to 3 per cent in 1995 as a result of accelerated growth in France, Germany and Italy. However, owing to some slowing of growth in the United Kingdom of Great Britain and Northern Ireland, the United States of America and several other industrialized countries, the average rate of growth for all industrial countries decelerated slightly. The average rate of economic growth in the developing countries also decelerated slightly, largely because of a sharp deceleration in Latin America. On the other hand, the rate of output decline experienced by the economies in transition over the past several years slowed substantially. This outcome reflected the positive rates of economic growth posted by several economies in Eastern Europe.

2. The short- to medium-term prospects for the world economy remain optimistic. Current forecasts show world economic growth accelerating to rates above 3 per cent in 1996 and 1997. Japan's economy, which has registered insufficient recovery so far, was expected to recover fully, with a growth rate of at least 2 per cent in 1996. An improvement in the average growth rates of both the industrialized countries and the developing countries is thus expected to push the world average rate of economic growth to above 3 per cent in 1996.

3. World output gains took place within a generally prevailing stable macroeconomic environment. The rate of inflation in the industrialized countries remained at around 2 per cent in both 1994 and 1995. Early in 1995, there was some apprehension that the high-speed economic recovery observed in several industrialized countries in 1994, particularly in Canada, the United Kingdom and the United States, could lead to a re-emergence of inflation. That could prompt a sharp policy brake to be applied, such as a raising of interest rates, that could prematurely abort economic recovery. This did not happen, however, and a slow but steady pace of economic growth in an environment of price stability has been achieved.

4. Continuing high rates of unemployment in most of the industrialized countries remain a matter of concern. The question arises whether the continuation of strict monetary policy regimes as anti-inflation measures could have retarded growth in investment, output and employment. Persistent large budget deficits in most industrial countries have also remained a constraint on the growth of savings and investments in the industrial economies. Whether a more liberal stance of monetary policy could have stimulated economic growth and reduced unemployment rates remains debatable. The prevailing high unemployment rates in the industrialized countries, however, tend to have adverse implications for international economic and trade relationships. Thus, imports, especially from the developing countries, are often blamed for the prevailing unemployment and are frequently the justification given by countries for seeking trade protection, although there is no firm evidence that international trade has any significant effect on unemployment rates in these countries.

5. The world economic recovery in 1994 and 1995 was accompanied by a rapid expansion in world trade. Thus, in 1994, the volume of world trade grew at 9.5 per cent, the fastest rate in many years. The rate of growth moderated somewhat in 1995 to an average of 6.9 per cent, a rate higher than any time between 1989 and 1993. Forecasts indicated similar high rates of growth during 1996 and 1997. Demand for imports in the industrialized countries, which account for around 70 per cent of world trade, has been the main determinant of overall growth in world trade volume. An expansion of imports in the developing countries, especially in Asia and Latin America, also contributed to growth in world trade. The rate of expansion in world trade has been faster than the rate of growth in world output in past years, resulting in a greater proportion of world output traded internationally. The recent rapid growth in world trade has further accelerated the process as part of an increasing globalization of economic activities.

6. Economic recovery and growth in world trade have had a favourable impact on the prices of several groups of non-fuel primary commodities. Prices of commodity groups such as tropical beverages, vegetable oil seeds and oils, and minerals and metals recovered substantially in 1994 and 1995 from the prevailing downtrend since 1989. The recovery, however, is not expected to be sustained over the medium term. Forecasts indicated slow successive declines in 1996 and 1997. The prospects of export earnings of commodity-dependent economies thus remain clouded.

7. Different forms of international private capital flows such as bond issues, equities, syndicated bank loans and foreign direct investments have registered considerable increase in recent years. Although the developing countries have received an increasing share of the total flows, their overall share in the total still remains relatively low, and most of the inflows remain concentrated in a small number of developing countries. There has been a decline in official development assistance flows to the developing countries over the past two years, which is a matter of concern for the world's poorest countries.

8. The growth and the current vast size of the international capital markets, along with the ease of capital mobility across borders, have come to exert considerable influence on national monetary and exchange rate policies, occasionally threatening the stability of either one or the other. That has required close coordination of macroeconomic policies among major industrial countries to prevent the harmful effects on national economies of any adverse market reactions to actual or perceived changes in national economic situations and associated policies.

9. Such policies have remained mostly anchored in maintaining monetary stability and fighting inflation. The exchange rate has thus borne the major burden of economic adjustments and short-term capital movements. The exchange rates among major currencies have therefore fluctuated considerably with worldwide repercussions. Countries failing to adjust in time have faced the risk of a crisis brought on by market reactions to any prevailing maladjustments, as was illustrated by the Mexican peso crisis late in 1994.

10. The recent developments in the world economy have had a positive impact on the developing countries of the Economic and Social Commission for Asia and the

/...

Pacific (ESCAP) region in several ways. The ending of the recessionary downturn in the industrial countries has favourably affected the growth in exports from the region, which is of crucial importance to these economies. The region has also received a considerable inflow of foreign direct investment and other financial flows, although these remained mostly concentrated in a few countries. The recent decline in international interest rates will reduce borrowing costs and further induce capital inflow.

11. However, several concerns remain. These include the speedy implementation of the agreements reached at the Uruguay Round of multilateral trade negotiations and a satisfactory resolution of pending trade-related issues. The declining trend in official development assistance has been a major concern to a large number of disadvantaged economies of the region. The increasing globalization of financial markets, to which the markets of the region's developing countries are becoming increasingly linked, poses new policy challenges to prevent externally induced instability in the domestic economy. The recent fluctuations in exchange rates among major international currencies have also evoked concern, though their adverse impacts have generally been limited.

II. MACROECONOMIC PERFORMANCE AND POLICIES IN THE ESCAP REGION

12. The economies of the developing ESCAP region in South Asia, South-East Asia and East Asia had yet another year of strong economic growth performance in 1995. Their average rate of growth had, however, decelerated slightly from 8 per cent in 1994 to an estimated 7.8 per cent in 1995. A further small deceleration is expected to continue through 1996 and 1997, partly to allow some of the economies a breathing space to overcome constraints (such as shortages of labour, skills and infrastructure) that have emerged as a result of years of rapid growth.

13. Among the East Asian economies, China's economic growth rate slowed from 11.8 per cent in 1994 to 10 per cent in 1995, while that of Hong Kong remained stable at 5.5 per cent. The Republic of Korea, on the other hand, had an accelerated growth rate at 9.3 per cent in 1995 compared with 8.4 per cent in 1994. Mongolia, an economy in transition, achieved a remarkable economic recovery with rates of economic growth of 2.1 and 3.5 per cent in 1994 and 1995, reversing the output contraction that the economy experienced in the early 1990s (table 1).

14. In South-East Asia, the average rate of growth accelerated slightly from 7.9 per cent in 1994 to 8 per cent in 1995 largely because of the noticeably better performance of the Philippines and Viet Nam. With the exception of Singapore, which experienced a percentage point drop in its growth rate in 1995, other countries of the subregion sustained or slightly accelerated the rates of growth in 1995 compared with those in 1994. Five of the South Asian countries maintained a moderate rate of growth, averaging 5.5 per cent in 1995.

/...

Table 1. Selected economies of the ESCAP region: growth rates and inflation, 1993-1995

(Percentage)							
		Gross domestic product	Inflation Rate <u>a/</u>			Gross domestic product	Inflation rate <u>a/</u>
<u>Least developed countries</u>				<u>Pacific island economies (cont'd)</u>			
Bangladesh	1993	4.5	1.3	Tuvalu	1993	8.7	1.5
	1994	4.6	1.8		1994	2.6	1.5
	1995	5.0	4.0	Vanuatu	1993	4.0	3.6
Bhutan	1993	6.3	13.6		1994	2.0	2.3
	1994	6.5	9.7	<u>Economies in transition <u>d/</u></u>			
Cambodia	1993	4.3	114.3	Armenia	1993	-9.9	1098.0
	1994	4.9	26.1		1994	-2.0	5060.0
Lao People's Democratic Republic	1993	5.9	7.4		1995	5.2	280.0
	1994	8.0	6.7	Azerbaijan	1993	-13.5	1230.0
	1995	7.0	16.0		1994	-17.2	1760.0
Maldives	1993	6.2	20.2		1995	-17.4	510.0
	1994	5.5	20.0	Kazakhstan	1993	-12.8	1760.0
Myanmar <u>b/</u>	1993	5.9	31.8		1994	-25.0	1980.0
	1994	6.8	24.1		1995	-8.9	280.0
Nepal	1993	2.9	8.9	Kyrgyzstan	1993	-17.4	1290.0
	1994	7.0	8.9		1994	-26.0	380.0
	1995	2.6	8.0		1995	-6.2	150.0
<u>Pacific island economies</u>				Russian Federation	1993	-12.0	940.0
Cook Islands	1993	1.7	7.3		1994	-15.0	320.0
	1994	1.5	2.8		1995	-4.0	230.0
Fiji	1993	1.8	5.2	Tajikistan	1993	-21.0	2240.0
	1994	5.2	1.2		1994	-12.0	340.0
	1995	2.7	..		1995	-12.4	500.0
Kiribati	1993	-2.8	6.1	Turkmenistan	1993	7.8	1730.0
	1994	-0.4	5.1		1994	-12.0	2810.0
	1995	..	..		1995	-7.5	..
Papua New Guinea	1993	16.6	5.0	Uzbekistan	1993	-3.5	1330.0
	1994	3.0	2.9		1994	-4.0	1650.0
	1995	-4.6	16.1		1995	-0.5	420.0
Samoa	1993	6.0	1.8	<u>South Asia</u>			
	1994	-7.1	18.4	India	1993	4.3	7.3
Solomon Islands	1993	4.4	9.2		1994	5.3	10.3
	1994	4.2	13.0		1995	5.7	8.0 <u>e/</u>
Tonga <u>c/</u>	1993	2.8	3.1	Iran (Islamic Republic of)	1993	5.0	22.9
	1994	5.7	2.4		1994	3.0	35.2
	1995	..	..		1995	5.1	..

/...

Table 1. (continued)

		(Percentage)					
		Gross domestic product	Inflation Rate a/		Gross domestic product	Inflation rate a/	
<u>South Asia (cont'd)</u>				<u>East Asia</u>			
Pakistan	1993	2.3	9.7	China	1993	13.4	14.7
	1994	3.8	11.2		1994	11.8	21.7
	1995	4.7	12.9		1995	10.0	15.0
Sri Lanka	1993	6.9	11.7	Hong Kong	1993	5.8	8.5
	1994	5.6	8.4		1994	5.5	8.1
	1995	5.4	9.1		1995	5.5	8.5
<u>South-East Asia</u>				<u>Mongolia</u>			
Brunei Darussalam	1993	0.5	4.3	Republic of Korea	1993	-1.7	268.4
	1994	1.8	2.4		1994	2.1	87.6
Indonesia	1993	6.5	9.2		1995	3.5	28.0
	1994	7.3	9.2	Developed economies	1993	5.8	4.8
	1995	7.1	10.0		1994	8.4	6.2
Malaysia	1993	8.3	3.6		1995	9.3	5.0
	1994	9.2	3.7	Australia	1993	4.0	1.8
	1995	9.6	3.5		1994	4.9	1.9
Philippines	1993	2.1	7.6		1995	2.1	4.6
	1994	4.3	9.0	Japan	1993	-0.2	1.2
	1995	5.3	8.1		1994	0.6	0.7
Singapore	1993	10.1	2.3		1995	0.7	0.0
	1994	10.1	3.1	New Zealand	1993	5.0	1.4
	1995	9.0	2.2		1994	4.3	1.7
Thailand	1993	8.2	3.3		1995	2.2	2.3
	1994	8.5	5.0				
	1995	8.6	5.8				
Viet Nam	1993	8.1	5.3				
	1994	8.8	14.4				
	1995	9.5	14.9				

Sources: International Monetary Fund, *International Financial Statistics*, vol. XLVIII, No. 9 (September 1995) and *World Economic Outlook* (October 1995); *Economic and Social Survey of Asia and the Pacific 1995* (United Nations publication, Sales No. E.95.II.F.10); Asian Development Bank, *Key Indicators of Developing Asian and Pacific Countries 1995* (Oxford University Press, 1995) and *Asian Development Outlook 1995 and 1996* (Oxford University Press, 1995); Intra-State Statistical Committee of the Commonwealth of Independent States (Moscow), *Economy of the Commonwealth of Independent States in 1995: Express-Review* (January 1996); and national sources.

Note: Data for 1994/1995 are estimates.

a/ Refers to changes in the consumer price index.

b/ GDP at 1985/86 producer's prices.

c/ Real GDP at factor cost.

d/ GDP or net material product.

e/ Estimate based on changes in the wholesale price index.

15. The further small deceleration in the average growth performance of these economies in 1996 and 1997 is expected to come largely from a slow-down in China and the Republic of Korea and a marginal deceleration in the South-East Asian economies. China's economic growth rate is expected to stabilize around 9 per cent in 1996 and 1997; that of the Republic of Korea could also drop by at least two percentage points. The average growth rate in the South-East Asian economies could also be marginally lower at 7.6 per cent compared with the 8 per cent rate of growth in 1995. The average rate of growth in the South Asian economies, on the other hand, is expected to accelerate moderately from 5.5 per cent in 1995 to above 6 per cent in 1996 and 1997, with a slow rise in the growth rates in India and Sri Lanka and a considerably improved rate of growth in Pakistan. The three developed countries of the region are also expected to improve their average growth performance in 1996 and 1997 principally as a result of a full recovery in the Japanese economy (table 2).

16. The performance and prospects of the region's least developed countries, the Pacific island economies and the economies in transition have remained less than satisfactory in most cases. Some of the least developed countries such as Bangladesh, the Lao People's Democratic Republic and Nepal have improved their growth performance in recent years but, for most of them, the rates of growth fell far short of what is required to alleviate their extreme economic hardship. In the Pacific island economies, with a few exceptions, growth rates hardly exceeded 2 per cent and their vulnerability to exogenous shocks remained as serious as ever. The economies in transition, especially those of Central Asia and the Russian Federation, continued to suffer from a severe economic plight as most of them were still experiencing output contraction in 1995. However, the rate of decline in comparison with earlier years became pronouncedly less, and some of them even showed positive signs of a recovery towards the end of 1995 that could last into 1996 and beyond. The most spectacular appears to have been the success of Armenia in posting a high positive rate of growth in 1995.

17. Macroeconomic stability and containment of inflation have been a concern for all groups of economies in the region, although the nature and intensity of the problems encountered by various groups of economies differed widely. The average rate of inflation among the developing countries listed in table 2 fell by two percentage points in 1995 from the previous year as most countries put in place anti-inflationary policies. In South Asia, the average rate of inflation has been coming down as a stronger commitment to economic reform and stabilization is gaining hold. Except in Bangladesh, however, the rates remained relatively high, and the average rate of inflation above 8 per cent is likely to persist at least into 1996.

18. In South-East Asia, the average rate of inflation is expected to remain within the 5 to 6 per cent range, with considerable divergence among individual economies. Inflation rates in Malaysia, Singapore and Thailand have traditionally remained low. Some acceleration in 1994 evoked prompt policy responses in all three countries to restrain inflation to levels where it could not pose a serious threat. The Philippines achieved success in reducing its inflation rate to a single-digit level in 1994. It is expected to go down further to 8 per cent in 1995 and lower in the next two years. Although the inflation rate in Indonesia appeared to have accelerated by a percentage point in 1995, owing to high demand pressures and the upward adjustment of some

/...

Table 2. Selected economies of the ESCAP region: forecasts of growth rates of gross domestic product and inflation, 1996-1997

	Real GDP		Inflation ^{a/}	
	1996	1997	1996	1997
<u>Developing economies of the ESCAP region ^{b/}</u>	7.4	7.2	7.6	7.0
<u>South Asia</u>	6.2	6.3	8.6	8.0
Bangladesh	5.0	5.0	5.5	5.0
India	6.3	6.3	8.5	8.0
Nepal	6.3	...	7.0	...
Pakistan	6.5	5.8	11.0	10.0
Sri Lanka	5.7	6.5	8.1	9.0
<u>South-East Asia</u>	7.6	7.6	5.9	5.7
Indonesia	7.0	7.2	8.0	8.0
Malaysia	8.5	8.6	4.2	3.8
Philippines	6.4	7.1	7.5	7.0
Singapore	7.3	7.0	2.5	2.6
Thailand	8.4	8.2	5.6	5.0
Viet Nam	9.9	10.6	15.3	16.4
<u>East Asia</u>	8.2	7.7	9.3	8.3
China	9.5	9.1	13.0	11.6
Hong Kong	5.0	4.8	8.0	7.6
Republic of Korea	7.2	6.6	4.5	4.0
<u>Developed economies of the ESCAP region</u>	2.1	2.3	1.0	0.5
Australia	2.8	2.3	4.2	2.7
Japan	2.0	2.3	0.7	0.3
New Zealand	3.7	3.5	1.3	0.9

Sources: Asian Development Bank, *Asian Development Outlook 1995 and 1996* (Oxford University Press, 1995); United Nations, Department for Economic and Social Information and Policy Analysis, "Project LINK World Outlook", 16 November 1995; and national sources.

Note: The forecasts for countries relate to fiscal years defined as follows: financial year 1996/97 = 1996 for India; financial year 1996/97 = 1997 for Bangladesh, Pakistan and Nepal.

^{a/} Refers to changes in the consumer price index.

^{b/} Based on data for 16 developing economies (including Papua New Guinea and Taiwan Province of China) representing more than 95 per cent of the population of the region (excluding the Central Asian republics); GDP at market prices in United States dollars in 1990 have been used as weights to calculate the regional and subregional growth rates.

administered prices, it is expected to slow down to 8 per cent next year as policies were being tightened to check price rises. Inflation in Viet Nam accelerated considerably from its low levels of 1992 and 1993 and was expected to remain in the range of 15 per cent in 1995 and 1996.

19. China's high rates of inflation impacted on the average rate of inflation not only in the East Asian economies but in the whole group of developing countries in the region. However, China succeeded in bringing down the inflation rate to the targeted 15 per cent in 1995 from 21.7 per cent in 1994, and it is expected to reduce it further in 1996 and 1997. The high inflation rate in China had an obvious impact on prices in Hong Kong, which recorded an inflation rate of 8.5 per cent in 1995. In the Republic of Korea, inflation had declined by more than a percentage point in 1995 to 5 per cent and is expected to fall by yet another percentage point in the next two years.

20. Apart from Bangladesh, inflation rates remained quite high in the least developed countries. However, Bhutan, the Lao People's Democratic Republic and Nepal have succeeded in bringing down their inflation rates to a single-digit figure. In Cambodia, Myanmar and Maldives, on the other hand, the rates exceeded 20 per cent, despite the fact that the rates in Cambodia and Myanmar had dropped substantially. With a few exceptions, the Pacific island economies succeeded in containing inflation, assisted by low inflation rates in Australia, New Zealand and the United States, their major trading partners.

21. The hyperinflationary price escalations in the economies in transition, especially in Central Asia and the Russian Federation, slowed somewhat in 1994 and the early part of 1995, but inflation remains a fundamental challenge to their reform and restructuring efforts aimed at establishing market-oriented economic regimes. Chronic budget deficits with liquidity overhang, coupled with supply shortages, continue to feed the inflation process that burst out with the initial moves towards economic reform in the early 1990s.

22. The fast-growing economies of East and South-East Asia have succeeded in sustaining high and rising rates of domestic savings and investment. Some of these economies have already become net exporters of capital. In most of the others, the gap between domestic savings and investment is relatively small and it has been financed largely by foreign direct investment, supplemented by portfolio investment, as well as commercial borrowings. That has enabled these countries to limit their external indebtedness. However, in a few cases, the recent deterioration in the balance of payments and a rise in the servicing costs of yen loans, as a result of the sharp appreciation of the yen, have caused some concern.

23. With the exception of China and Viet Nam, the budgetary situation in most countries in East and South-East Asia has remained healthy and strong. Hong Kong, Singapore and Thailand have been experiencing budget surpluses for several years, while a number of other countries have recorded surpluses during the past two years. The success of the Philippines in achieving a budget surplus, despite a heavy load of debt-servicing costs, is remarkable. Indonesia has operated within the framework of a balanced budget concept with any excess of expenditure over domestic revenue being limited to the availability of external aid and credit, thus with no scope for internal borrowing to finance budget

deficits. The effective control over budgetary deficit is a factor that could largely explain the price stability that these countries have enjoyed.

24. The savings-investment process in South Asia, in contrast to the performance in East and South-East Asia, has remained relatively weak. This is usually also the case in the region's least developed countries and the Pacific island economies. In South Asia, the economic reform packages being implemented by various countries have succeeded in accelerating export growth, attracting larger volumes of foreign direct investment, increasing levels of foreign exchange reserves and reducing inflation rates. However, savings-investment rates seem to be stagnating in most countries. This may explain the insufficient acceleration in the growth rates of their economies.

25. In Bangladesh, national saving rates accelerated to reach 13 per cent of GDP in 1994, doubling from the rate prevailing at the beginning of the 1990s, a remarkable feat in itself. That, however, has not translated into similar acceleration in the rates of investment in the economy. The relatively high rates of investment in the economies of Nepal and Sri Lanka, on the other hand, left wide gaps between the investment rates and domestic savings rates. Foreign aid, and credit flows required to fill them, may not be sustained for long. In India and Pakistan, the savings-investment rates seem to have remained relatively stable. The rates in India have tended to stabilize at a relatively high level for some time. In Pakistan, a similar stability of investment rate at a slightly lower level prevailed. Despite recent efforts to enhance revenue mobilization through major tax reform and contain growth in government expenditure, budgetary deficits remained high in both countries.

26. The savings-investment scenarios in the Pacific island economies and the economies in transition are not very clear. Savings-investment data are not available or are unreliable for most of these economies. Scattered information suggests that some of these economies have recently succeeded in attracting sizeable amounts of foreign direct investment which, however, have not yet made much of a difference in their otherwise weak economic performance. Large budgetary deficits have continued to be a feature of almost all these economies as their revenue potential remains weak, or yet unrealized, while expenditure commitments cannot be reduced.

27. Notwithstanding the differences in actual outcomes and achievements, almost all the countries in the region have shown their strong commitment to reform, the restructuring, stabilization and liberalization of their respective economies. Reforms have encompassed monetary and fiscal institutions and instruments, as well as the regimes of administrative regulations and controls affecting both the real and financial sectors of the domestic economy. Expanding the role of the private sector in the economy, including programmes of privatization of public enterprises and accelerated measures of liberalization of trade and investment regimes, has been the cornerstone of most reform programmes. The differences that continue to show up in the actual macroeconomic performance of the various economies of the region reflect the initial conditions from which the reforms were initiated, the length of time over which the measures have been implemented, the responsiveness of different economies determined by their resource endowment and technological capabilities,

and a host of other factors. The process of reform continues nevertheless in most countries.

III. INTERNATIONAL TRADE AND BALANCE OF PAYMENTS

28. International trade is a crucially important element that has propelled the economic dynamism of the developing countries in the ESCAP region. With few exceptions, countries continue to emphasize the importance of international trade in their economies and to evolve policies to participate more fully in the expected expansion in trade in the post-Uruguay Round environment. While emphasizing export promotion, most countries are taking steps to liberalize their import regimes by reducing tariffs and removing administrative controls, as well as other forms of non-tariff barriers. These reflect not only their commitment under agreements reached in the Uruguay Round of multilateral trade negotiations but also in various subregional forums such as the Association of South East Asian Nations and Asia-Pacific Economic Cooperation.

29. The latest available statistical data confirm that growth in both exports and imports for most of the developing countries in the region has remained buoyant. The export values for the region's developing countries on an average grew at 14 to 15 per cent even during the worst recession years of 1991 and 1992. Similar but slightly lower rates of growth were recorded for imports. Stimulated by the broad-based recovery in major export markets, the rate of growth in the dollar value of exports from the developing countries of the region accelerated to almost 20 per cent in 1994, while the growth rate of imports accelerated to more than 18 per cent. The 1995 data available for a limited number of countries indicate that both exports and imports continue to grow strongly, although the rate of growth overall could be somewhat slower than in 1994.

30. As in other areas of economic performance, the weakness of the region's least developed countries, the island economies and most of the economies in transition is also exposed in the field of trade and balance of payments. Several of the least developed countries in the region, such as Bangladesh, Cambodia, the Lao People's Democratic Republic and Myanmar have achieved impressive rates of growth in exports. These apparently high rates of growth are, however, based on very small bases, which in terms of GDP share also constitute a very small part of each individual economy. The high rates of export growth therefore do not create a sufficiently broad dynamic impact on these economies. The narrow commodity base of the export trade, limited either to a few primary commodities or simple manufactured goods such as textiles and garments, constitutes a further structural weakness of their trade.

31. The balance of payments of these economies also remains structurally unbalanced in most cases. Imports generally exceed exports by a margin of at least two to one. The resulting trade deficits are, with a few exceptions, further aggravated by the deficits incurred in the trade in invisibles. Recent developments have also indicated a deterioration in the balance of trade and payments of a number of the well-performing economies of the region. These include India, Indonesia, Malaysia, Pakistan, the Philippines, the Republic of Korea, Sri Lanka and Thailand. Very high rates of growth in imports worsened

/...

the deficits in the trade balances of several of these countries in 1995. There were also larger deficits in invisibles, particularly on account of the costs of servicing external debts and payments related to foreign direct investment in these countries. China and Singapore enjoyed a comfortable balance-of-payments situation, with surpluses recorded in both their merchandise and their invisible trade accounts. Continuing strong inflows of capital, however, have enabled the deficit countries not only to finance the payment deficits but also to build up their reserve assets.

32. The balance-of-payments situation has raised concerns in several countries. The continuing liberalization and openness of trade regimes, as well as easier access to credit and capital, including offshore facilities, may be encouraging a rapid growth of imports. Exports, on the other hand, are facing more intense competition based on differences in costs and efficiency. Several countries in the region have been experiencing labour and skill shortages, and consequently higher labour costs of production, thereby losing comparative advantage in producing simple manufactured goods based on cheap labour. These countries will have to shift their industrial and production structures towards more technology-intensive areas and improve labour productivity in existing industries. The existence of cheap labour in low-wage countries is also no guarantee that they will be able to compete effectively in the international markets. Unit production costs in the low-wage countries may still remain high if low productivity offsets low wages.

33. The management of the balance of payments in the new, open and deregulated trade and financial environments poses new challenges. The market may be relied on to know better, but the market can also be misinformed or it can misread the indicators of economic fundamentals in a given situation or react to well-intended policy moves in perverse ways. Thus, a run on a country's balance of payments can be induced by purely speculative moves. A short-term balance-of-payments crisis may, however, also ensue as a matter of course. Industrial countries, which decontrolled and freed their balance-of-payment transactions in earlier decades, have devised various individual and collective mechanisms to protect individual economies from such adverse developments. The countries in the ESCAP region have also shown awareness of the potential risks involved in the new openness of their trade and financial regimes. That awareness was reflected in a series of understandings recently reached among central bankers in the region to provide mutual assistance and credit line offers to each other in times of any such critical developments. That, however, would not diminish the need for vigilance on the part of the guardians and managers of policies in individual countries.

IV. ENHANCING THE ROLE OF THE PRIVATE SECTOR IN DEVELOPMENT

34. In all countries of the ESCAP region, the private sector is viewed as a key instrument for achieving economic goals in a world of rapidly increasing global competition as it is considered to be more efficient, flexible and productive than the public sector in undertaking a large variety of investment, production, distribution and service-related activities. There is a consistently visible emphasis across countries on policy reforms which are either directly or indirectly designed to encourage the development of the private sector and to

enhance its role in economic activities. The role of Government is thus being transformed from being mainly a provider to being an enabler in the production and distribution of goods and services. However, the success of the policies followed depends on the underlying preconditions for private sector development, including stable and credible political conditions, law and order, and the continuity of policies which in themselves must be credible, consistent and transparent, as well as stable macroeconomic conditions. Policies take time to implement, with their results often not being visible in the short run, and the private sector needs to be confident that policies will not suddenly be reversed. Success is predicated on the ability of the State actually to implement the policies adopted: the lack of effective implementation, which is visible in many countries in the region, is often related to a lack of political will, a lack of reform of the public administration to increase its efficiency and the influence of vested interest groups in both the public and the private sector. Thus, building a firm foundation for private sector development depends crucially on the role of Government in creating an enabling institutional environment and in implementing an efficient set of promotional policies.

35. One fundamental role of Government is to develop and manage a sound and credible legal framework for private sector activities. High transaction costs for the private sector in many developing countries are often associated with risks and uncertainty emanating from undefined property rights systems and problems of contract enforcement. Private ownership of property is a core institution in an economy with a vibrant private sector since it provides the incentive for property owners to engage in various transactions in order to maximize the economic value of their property. There is still considerable scope for improvements in the systems of property rights and the functioning of land markets in the region. This requires greater attention.

36. Contract enforcement is closely associated with the implementation of property rights. Without some form of assurance that the purchasing or selling of contracts into which they enter will normally be honoured, and if they are not, that there is a legal recourse, private sector entities have no firm basis on which to initiate activities. Countries with strong, credible regimes for enforcing contracts for investment and trade or in the financial sector, such as in the East Asian countries, are more able to achieve the rapid and sustainable growth of their private sector. While devising a complete and consistent commercial legal system is important, no less so is the mechanism of governance and implementation. There is ample evidence that a weak bureaucracy, coupled with an ineffective judicial system, tends to generate an inefficient implementation of the formal institutional structure.

37. The deregulation and liberalization policies being implemented by countries in the region are aimed at getting prices and incentives right and, in so doing, they underwrite the enhancement of the role of the private sector in an economy. All countries in the region, including those that previously practised pervasive administered prices, have abolished many of the controls on prices of both inputs into and outputs from the production process. However, administered or indicative maximum or minimum prices still exist in many countries of the region for selected agricultural exports or basic foodstuffs with the rationale of protecting the interests of the small farmers and the poor. At any rate, these administered prices should be highly selective and generally time-bound.

/...

38. Fiscal reforms also form a major component of deregulation in practically all countries in the region. While these are often intended primarily to affect government budget positions, their content has significant implications for the private sector. Many changes in tax rates and in the structure of the tax systems have been designed to improve the incentive structure facing the private sector, either by reducing direct tax on business income or by rationalizing and simplifying the tax structure for corporations. In countries where tax reforms were undertaken some years ago, there is now a concern to keep the structure relatively stable so as not to create uncertainty for the private sector.

39. Financial sector deregulation and liberalization can also assist in providing the necessary stimulus to private sector development. Interest rate deregulation, which is ongoing in most countries, can contribute by allowing interest rates to rise and so increase the supply of loanable funds. Reducing or eliminating programmes of directed or subsidized credit helps to reduce fragmentation in the financial market and to make the competition for funds within a country more transparent and equal. Similarly, the ongoing reforms to reduce entry barriers of financial institutions and to widen the financial services available should help to increase competition in the provision of credit to the private sector and to widen the choice of ways to raise funds.

40. A major distortion facing the private sector in many developing countries emanates from a commercial policy that is protective of local industry. A major task of recent reforms, therefore, has to do with dismantling the various barriers in the areas of trade and investment. Liberalization in trade regimes has been escalating in the region, encompassing almost all economies and sectors within each economy. The results of creating competitive conditions and accelerating the growth of the private sector have been mixed, however, and depend crucially on the initial conditions of the country. Countries with strong and stable macroeconomic fundamentals, such as those in the East and South-East Asian regions, have exhibited substantial gains in growth and exports, including those from the private sector over the past 10 years, as a result of massive deregulation and liberalization policies. Further trade liberalization is likely to involve further curtailing and rationalizing of tariff rates and reductions in non-tariff barriers, as well as addressing the problem of barriers in the politically sensitive area of agriculture.

41. Governments have come to realize the strategic importance of foreign investment in supporting the development of the private sector, as partners and as competitors, and as role models for domestic private firms in terms of structure, procedures and management practices. All countries in the region have undertaken significant measures aimed at liberalizing investment regimes and yet direct foreign investment inflows remain concentrated in a few countries. The reasons for this include the credibility of the regulations and the enforcement regimes within which the private sector operates.

42. While deregulation and liberalization reduce entry and credit barriers for private firms, they need to be complemented by an effective competition policy. The crux of such a policy is to protect the economy and the public from various forms of abuse of market power. In a formal sense, most countries in the region either have legislated a competition law or have provisions on fair trading in their commercial legal structure. However, the actual practice of enforcing

competition policies is very weak and uneven, and much remains to be done in this area.

43. Creating an enabling environment for private sector development is necessary but not sufficient; it needs to be supplemented by promotional policies to develop entrepreneurship, to build up technology capabilities and to improve access to finance. Management education and training are essential to enhance entrepreneurship development. While the list of government-sponsored management training schemes in the region is endless, there is a need to improve the schemes, in close cooperation with the private sector, in order to take the needs of the private sector more into account. Fostering inter-firm linkages and other modes of learning-by-doing for managers are also useful ways of enhancing entrepreneurship. The role of Government in building up technological capabilities is often crucial through, for example, exposing firms to international competition, emphasizing science and technology in education, and fostering research and development activities.

44. There appears to be room for improving the access to finance for investment by small and medium-sized enterprises without contradicting efforts to liberalize the financial sector. Experience shows that lending rates should be charged at the prevailing market rates, but efforts are needed to reduce transaction costs by simplifying paperwork and improving conditions for collateral. The latter problem can be addressed through activities of business associations, subcontracting arrangements and training on keeping accounts and risk assessment.

45. At present, there is a plethora of government policies and action programmes to support private sector development in the region, each directed to certain goals and certain target groups and many directed specifically to the development of small and medium-sized enterprises. The effective management of the programmes as a whole to ensure synergy among various programmes and institutions is important. To accomplish this, Governments need to foster closer cooperation with the local private sector through various forms of consultative mechanisms. Experience with government-business consultancy forums in Malaysia, the Republic of Korea, Singapore and Thailand is instructive as it provides many useful lessons for making policies and programmes more responsive to changes in the business environment. Business associations can also play an important role as a conduit of legitimate business interests.

46. The provision of adequate economic infrastructure services provides an enabling condition so that it is possible for the private sector to undertake business activities. In targeted schemes such as those in special economic zones, it actively encourages private sector activities by providing them with a relatively dense network of infrastructure services that would have been too expensive to build over a larger area. The need for a policy framework to increase the provision and improve the performance of infrastructure services has been recognized in most countries in the region. Indeed, the demand for economic infrastructure is increasing much more rapidly than its supply for reasons of rapid economic growth, urbanization and poor infrastructure maintenance. Even though government finance will still be the most important source of infrastructure financing, the private sector can and is being

encouraged to take over certain functions such as the building of, or management of, many forms of infrastructure.

47. Taking measures to enhance the role of the private sector in economic activities also creates a new series of problems and issues which need to be addressed. One challenge is to cope with the potential short-run destabilizing effects of deregulation and liberalization on macroeconomic fundamentals. Deregulation and liberalization actions have significantly increased the interdependence among the macroeconomic variables and eroded the capacity of national authorities to exercise effective control over all these variables simultaneously, as well as significantly changing the tools at their disposal. Thus, while the need to ensure a stable and predictable macroeconomic environment has become greater as countries rely to a larger extent on the private sector for development, the task of macroeconomic management has at the same time become more complex, requiring much more information, knowledge and skill.

48. The need for continuing institutional reform will persist in all countries. With the increasing relevance of competition policy in managing a competitive economy based on the private sector, a pressing need emerges for each country in the region to legislate viable laws governing the potential abuses of market power. Developing a tradition of transparency in transactions of private firms, especially larger ones, is another emerging concern. In addition, Governments cannot be oblivious to the importance of equity. Even if strategy based on the private sector is efficient, there is nothing inherent in the system to assure equitable distribution of the fruits of production and to lead to alleviation of poverty. Here again, some form of government intervention may be unavoidable. Governments have to decide on a proper mix of efficiency and equity according to the needs and circumstances of individual countries.

V. THE ROLE OF PUBLIC EXPENDITURE IN THE PROVISION OF SOCIAL SERVICES

49. The developing countries in the ESCAP region are increasingly recognizing the crucial role that human and social development plays in overall national development, as well as in enhancing people's welfare. Despite the substantial progress made over the past decades, there are still significant lags in many areas of social development and the services available to broad segments of the population. Demand for more and better social services is also increasing. These demands need to be met efficiently and equitably.

50. Traditionally, the public sector has been given a prominent role in the production and delivery of social services on the grounds of both efficiency and equity. The efficiency argument runs on considerations of the externalities involved in the production and consumption of social services, which could best be captured through public sector rather than through profit-oriented private sector actions. The public provision of social services can easily incorporate positive discrimination in favour of the poorer segments of society and therefore help to improve income distribution and reduce poverty. The public sector continues to play a major role in the provision of social services

throughout the region, despite recent calls for the greater involvement of the private sector in these activities.

51. The importance attached to social development and social services by countries in the region is reflected in the public resources devoted to the production and delivery of social services in areas such as education, health, housing, water supply and sanitation, and social protection. Over the past two decades, expenditure on social services has constituted between a fifth and a third of total government budgetary expenditure in most of the countries of the region, irrespective of their level of development. Since the beginning of the 1990s, there has been a steady rise in the proportion of public expenditure on social development in most of the countries. With the exception of a very few countries, the proportions of public expenditure allocated to social sectors now exceed 20 per cent. Expressed as a share of GDP, expenditure on social services generally ranges from 5 to 10 per cent. There are, however, countries which still spend less than 5 per cent of GDP on social sector developments and social services and some of them are the region's least developed countries.

52. The relatively high levels of social expenditure, as reflected in the share of total spending as well as of GDP, conceal the inadequacies and inequities of intra-social sector allocations of resources. In many countries, the major shares of educational expenditure, for example, are devoted to higher levels of education rather than primary education, even when primary enrolment ratios are low and illiteracy rates are high. Similarly, in the area of health care, more emphasis is placed on expensive hospital-based curative health care, and relatively less on preventive and promotive services which could easily remove some of the leading causes of morbidity and mortality.

53. Nevertheless, in practically all countries of the region, there have been considerable accomplishments in the field of education, health, water supply and sanitation over the past few decades. Numbers of schools, teachers, hospitals, doctors and other relevant institutions and personnel have increased, for example. Public health and sanitation programmes have been expanded in most countries to cover the major proportion of the population. The increased accessibility to the various services is reflected in the relevant indicators, such as a rise in enrolment ratios and literacy rates and an extension of life expectancy through reductions in morbidity and mortality.

54. There are still quantitative and qualitative deficiencies in many areas of the social services. In the field of education, for example, enrolment rates are still relatively low and drop-out rates are high in several countries. This particularly affects female and underprivileged children in rural areas and depressed urban locations. The quality of education often remains poor because of a lack of teachers and a poor supply of books and other educational equipment, even where schools exist. Similarly, in the area of health, infectious and communicable diseases remain a major health hazard, infant and maternal mortality rates remain high and public health coverage remains inadequate. A new public health hazard in the form of AIDS has emerged as a major threat.

55. Although there are very few benefit-incidence studies to locate precisely the costs and benefits of the expenditure on social services, it is almost

certain that the relatively well-off sections of society benefit more from the expenditure and the services provided. Access to the facilities and services is generally easier for the well-off than for the poor segments of both urban and rural residents.

56. It is obvious that both quantitative and qualitative improvements are necessary in many areas of social services in the region. These improvements can come about through the provision of more resources, as well as through a more effective use of the resources that are spent on them. Scope seems to exist for augmenting public resources that can be devoted to expand and improve the social service infrastructure, as well as to provide more and better services. Tax revenue can be enhanced through a greater rationalization of tax structures and a more vigorous enforcement of taxes to eliminate or minimize tax avoidance and evasion. User charges can be levied using the criteria of progression, making those who can afford to pay for services do so, while providing them free or at subsidized rates to those who cannot afford the costs. There are perhaps economies to be effected in several areas of public expenditure, such as on defence and general administrative services. The savings arising out of such economies could be reallocated to the social sectors.

57. The private sector, non-governmental organizations and local communities could be more actively involved in developing and maintaining social services facilities and in the actual delivery of many of the services. One way of encouraging private sector participation could be through a matching arrangement under which the public sector would complement, on a one-to-one basis, any private sector contributions to facilities that were developed and managed properly. Such arrangements would instil a sense of partnership between the public and the private sectors, allowing the former a stake in the necessary supervision of private activities.

58. Community involvement would encourage contributions from the community not only to build but also to maintain facilities and to regard them as their own. The administration of means-tested discriminatory pricing of services, as suggested above, would be easier and more efficient with community involvement. All these would require considerable decentralization and devolution of activities, resources and decision-making powers at local levels.
